CARANA
CORPORATION
Providing Global Development Solutions

UGANDA COFFEE SECTOR

REVIEW OF COMPETITIVENESS

STRATEGIES

Final Report

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Annexes

Acronyms

ABT – Abt Associates Inc.
ACDI-VOCA - Agricultural Cooperative Development International - Volunteers Overseas Cooperative Assistance
APEP - Agricultural Production Enhancement Program
CARANA – CARANA Corporation, Inc.
COMPETE– Competitive Private Enterprise & Trade Expansion
CORI – Coffee Research Institute
DFID – Department for International Development
EAFCA – Eastern African Fine Coffee Association
ECFA - Eastern Coffee Farmers Association
EU – European Union
GDP – Gross Domestic Product
GOU – Government of Uganda
ICRAF – International Center for Research in Agroforestry
IDEA – Investment in Developing Export Agriculture
MAAIF - Ministry of Agriculture Animal Industry and Fisheries
NGOs – Non-Governmental Organizations
PNG - Papua New Guinea
PRIME - Productive Resource Investments for Managing the Environment
PSFU – Private Sector Foundation Uganda
RATES - Regional Agricultural Trade Expansion Support Program
RSPB - Royal Society for the Protection of Birds (UK)
SGC – Shade Grown Coffee
SMEs – Small and Medium Enterprises
SO7 – USAID Strategic Objective Number 7
SPEED – Support for Private Enterprise Expansion & Development
TA – Technical Assistance
UCDA – Uganda Coffee Development Authority
UCTF – Uganda Coffee Trade Federation
UCFA – Uganda Coffee Farmers Association
USDA-FAS - United States Department of Agriculture - Foreign Agricultural Service
USGS - United States Geological Survey
UTRADE –Uganda Trade Revitalization & Diversification of Exports Program
USAID – United States Agency for International Development

EXECUTIVE SUMMARY

The purpose of this report is to review Uganda's coffee sector competitive strategies that were agreed upon at the President's Conference on Competitiveness in February 2002 in Kampala. Additionally, the report examines how USAID's currently funded projects (IDEA, SPEED, EAFCA and RATES) can support these strategies and how future USAID resources can be directed (via UTRADE, PRIME and APEP) so as to address SO7 and further the coffee cluster's development.

Uganda's coffee sector is moving forward toward addressing the strategies that it laid out at the President's Conference in February 2002. One year after the conference, approximately half of the action areas that were identified by government, industry and donors have been addressed to some extent. Approximately 21 different action areas were agreed on, and all of these remain relevant, except the possibility of one (the proposed port set-aside area in Mombasa, Kenya, for Ugandan coffee exports).

Cluster stakeholders agree on what activities need to take place to move the sector forward; however, there is still considerable discussion on how implementation of certain activities should proceed. One of the most politically and financially important issues is the question of identifying new genetic material for the coffee sector, multiplying this material, and distributing it to farmers to replace old and diseased coffee bushes.

UCDA estimates that the coffee wilt pathogen kills about 5% of the nation's Robusta coffee bushes annually. At the current time, researchers have not identified a wilt tolerant/resistant Robusta genotype. It does not appear that a suitable resistant candidate will be available in the next three to five years. Given this fact, the cluster needs to agree on details of how to proceed with the replanting. One strategy is to replant with a newly identified Arabica PNG genotype that can be grown at low elevations, and thus can be used in many of the Robusta production areas. CORI is currently undertaking commercial trials of the PNG genotype.

As an alternative to coffee production, farmers in some areas where Robusta wilt is endemic may want to shift from a coffee production system to cocoa and vanilla. This will be possible in wetter coffee production areas, but in the drier areas, these alternative crops are not suitable.

Another issue in the replant program is how much of the crop should be replaced. The new Robusta clonal varieties have doubled the yield of the traditional varieties. If all of the traditional varieties were replaced with clonal, Uganda's coffee production would double. Given the over-supply on world commodity coffee markets, planners need to consider the impact of dumping additional coffee into this system.

Specialty coffee markets in the U.S. and Europe are growing by 20% per year. Prices for specialty coffees are far superior to those paid for commodity coffees. Less than 1% of Uganda's coffee exports are sold as specialty coffee. In the future, Uganda will be challenged with developing its specialty coffee production, and establishing itself in the world market as a known origin for fine coffees. This should be one of the key tasks targeted by UTRADE, PRIME, and APEP.

All members of the coffee cluster recognize the need to address poverty in Uganda. Reducing poverty is the key goal in USAID's coffee sector investments. Currently, nine of the 10 largest exporters of coffee in Uganda are owned by or controlled by multinationals. These nine firms control 80% of exports. USAID needs to develop ways to increase competitiveness in the sector, improve transparency and create more opportunities for local SMEs and farmer organizations in the coffee cluster. At the same time, USAID needs to work with its multinational coffee business partners to deliver technical assistance to the vast network of farmers who sell to these organizations.

Specifically, UTRADE, PRIME and APEP should link with the multinationals to implement activities in quality improvements at the farm level, and develop new products and markets (differentiated), such as shade grown coffee, semi-washed and fully washed coffees, coffee appellations, certified organic, and/or other products[1]. Equally important as working with the multinationals is the more challenging task of working with indigenous farmer groups and SMEs to provide them with expanded market opportunities. The local SMEs and farmer organizations will require much more TA in business skills training, quality assurance, market information analysis, risk management and many other critical areas that need to be mastered to successfully operate in the coffee sector. In short, working with the multinationals will be the easy part of the task; working with local organizations will be the most challenging yet most essential part of USAID's future investments in Uganda.

Developing Uganda's specialty coffee production and markets will be an incremental process. Production, market channels and promotion need to proceed on a parallel development schedule. To do this, USAID needs to focus resources on areas such as production certification programs, coffee auction development (market channel development) and market promotion. The decision on how to proceed with these activities should be the decision of the entire coffee cluster, but planners need to realize that there is a dichotomy of interests between multinational and local firms. Multinationals want better quality coffee, but their goal is to maximize profits rather than maximizing farmgate incomes. Where farmers and local firms would benefit from greater transparency, competitiveness and more market access, it is unlikely that the multinationals will see these as benefits. Issues such as the proposed coffee auction act as a touchstone between how local and multinational firms' view the development of the coffee sector. For USAID, the deciding question on whether to invest in activities such as specialty coffee development, the coffee auction and Ugandan coffee promotion activities should be if there is buy-in by the target beneficiaries and if the investment would reduce poverty.

[1] In May 2003, a DFID-funded study examining the marginal benefit of different certified coffee products will be released. This report should provide guidance to planners as to the best options available for increasing returns to the farmer per the various available certification programs.

Republic of Uganda

Uganda

- Population 24.7 million
- GDP $29 Billion
- Land Use
  - Arable land 25%
  - Permanent crops 9%
  - Other 66%

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Methodology

This report was prepared over a 24-day period between 1 January through 29 January 2003. The in-country field research took place from 3 January through 20 January and was followed by 6 days of data analysis and report preparation. The research included a complete review of the coffee cluster's background-operating environment, beginning with a review of documents prepared by NGO's, USDA-FAS, USAID-supported projects, as well as documents prepared by the GOU, German and British Governments and NGO's. The consultants also examined the export history of individual firms operating in Uganda's coffee sector and noted industrial trends.

In the course of the research, one-on-one interviews were conducted with private sector coffee traders and farmers, GOU Ministry of Agriculture Animal Industry and Fisheries (MAAIF) officials, Ministry of Finance officials, Uganda Coffee Development Authority management, coffee producer association representatives, USAID-funded project staff with activities in the coffee sector. In addition, USAID Uganda Mission staff with areas of responsibility in sustainable economic development, private sector development, natural resource, Food for Peace, and conflict resolution were also interviewed.

Acknowledgments

The preparation of this report would not be possible without generous assistance from Henry Ngabirano of the Uganda Coffee Development Authority and his staff. Thanks and appreciation also goes to John Byarugaba of the Uganda Coffee Trade Federation and Fred Kawuma of the Eastern African Fine Coffee Association for their support through the entire process of researching and preparing the draft document. Gratitude also goes to Moses Atwine, Uganda coffee specialist, for his direct and candid observations of the unique local operating environment. Finally, the consulting team expresses its appreciation to the USAID Uganda staff for freely contributing time and thought in the preparation of the following document.

Coffee Competitiveness Strategies In Uganda

1.0 Report Objective

SO7 – Expanded Sustainable Economic Opportunities for Rural Sector Growth: Key Results

- Increased food security for vulnerable populations in selected regions
- Increased productivity of agricultural commodities and natural resource systems in selected regions
- Increased competitiveness of enterprises in selected sectors
- Improved enabling environment for broad-based growth

The purpose of this report is to review the coffee sector competitiveness strategies in Uganda that were developed in February 2002 during the COMPETE Project's President's Conference on Competitiveness.

The report also examines ways to further develop public-private dialogue within Uganda's coffee cluster by reviewing the progress on implementing the strategic activities and determining their relevance one year after their proposal at the President's Conference on Competitiveness.

A third focus area of the report examines the activities of the USAID-funded SPEED, EAFCA, RATES and IDEA projects in Uganda, and makes recommendations as to how these activities can be directed so they support future USAID/Uganda investments in the coffee sector that target SO7 via UTRADE, PRIME and APEP.

2.0 Background

2.1 The World Coffee Market

The world coffee market volume is growing at approximately 3.6% per year. Consumption of coffee in the world is growing at approximately 1.6% per year. As a result of this dis-equilibrium in the market, coffee prices began falling in 1994 and continued a downward trend until mid-2002. This fall has been significant; in the 1994-95 season, the mean price for 1 kilo of coffee exported from Uganda was 2.58 USD. By the end of 2002, a kilo of Ugandan coffee was selling for 0.44 USD[2].

The specialty coffee market has performed significantly better than the commodity coffee market throughout the 1990's. In North America and Europe, the specialty coffee market is growing at 20% per year. Prices received for specialty coffees have fallen along with the commodity coffees, but their export values remain significantly higher than their commodity cousins. Bugisu AA, which is one of Uganda's specialty coffees, had an export value in the 4th quarter of 2002 of 1.31 USD/kg. This compares to a Robusta screen 15 commodity coffee export value from Uganda of 0.62 USD/kg. Uganda currently lacks significant volume in the specialty coffee sector. In 2002, less than 1% of Uganda's coffee exports could be considered specialty coffee.

[2] Mean provisional export value for all coffees exported from Uganda in 2002. In the 4th quarter of 2002, Robusta coffee price increased to approximately 0.62 USD/kg.

2.2 Coffee in the Ugandan Economic & Political Environment

The IMF estimates that the Ugandan GDP will have a real growth rate of 5.7% in 2002. This is slightly below the 6.0% GDP growth rate that had been projected. Part of the gap between the projected GDP growth rate and the revised number is the lackluster performance of the coffee sector. The low prices in the coffee sector have contributed to a 3% decline in total export earnings between 2001 and 2002.

Coffee in the Economy: In Uganda, it is estimated that 2 million people residing in 500,000 households depend on coffee for part of their household income. In many cases, coffee is their only cash crop, and pays for school fees, medicines and other essentials. In the 1994/95 season, coffee farmers in Uganda received approximately 303 million USD in sales revenue at the farmgate. In the 2001/2002-market year, sales at the farmgate were estimated to be below 70 million USD. These farmgate gross revenue figures are calculated under the assumption that farmers receive approximately 70% of total export value.

Historically, coffee has been Uganda's largest export. The UCDA and Bank of Uganda have not yet released final figures for 2002, but it is estimated that with the slight increase in coffee prices in the third and fourth quarters of 2002, total coffee export values may reach 100 million USD. As can be noted in Figure 1, coffee and fish exports were nearly at the same level in 2002. Assuming some improvement in market conditions in 2003, coffee should regain its position as the country's dominant export.

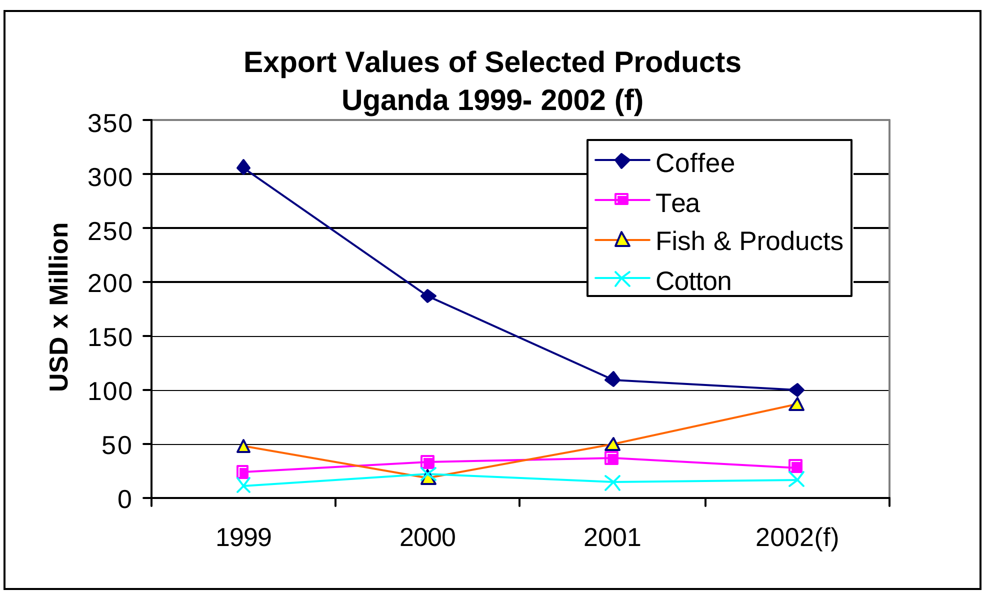

Figure 1, Source: Bank of Uganda, September 2002 and UCDA estimates end 2002.

Coffee and Politics: Given coffee's importance in the Ugandan economy, the sector also plays an important role in politics. The President of Uganda has made political promises to increase coffee production as a way of increasing rural incomes. On the surface, this may sound like a sensible approach; however, there are a number of issues that need to be considered before fully implementing this political promise.

Robusta coffee comprises approximately 85% of Uganda's coffee exports. The country's Robusta plant population is old and needs replanting. By some estimates, the average age of the Robusta population is 40 years. Usually, coffee bushes are replanted after 25 years. Older coffee bushes tend to be low yielding due to their weaker genetics (compared to more modern genotypes), as well as disease and insect pressure. There is a consensus among government, donors, and the industry that there needs to be large-scale replanting.

The new clonal coffee genotypes yield approximately double the old traditional varieties. Therefore, if all of the existing Robusta were replanted with new clonal material, Uganda's coffee exports would exceed 6 million bags. In 2002, exports were just over 3 million bags. By adding an additional 3 million bags on the world market, further downward pressure would be put on prices, and this would hurt coffee farmers worldwide.

The GOU needs to find a compromise position that will allow the President to deliver on his campaign promises without causing damage to the world coffee price. One compromise could be to move ahead with a moderate effort to replant old and diseased coffee bushes with new clonal varieties, and shift from a mix of 85% Robusta and 15% Arabica to a 70% Robusta and 30% Arabica replant mix. The UCDA has already indicated that this is a reasonable target, and is moving in this direction. In addition, farmers can be given the choice of planting cocoa rather than coffee in the higher rainfall areas. This will aid in diversifying the country's crop mix, and provide an economic shock absorber from some of the market shocks that have recently affected the coffee sector.

Politically, it is difficult for many of the administrators in the government to directly propose these types of alternatives to the President. Many bureaucrats feel that their careers would be shortened if they question the President's plan. Given this fact, donors can play an important role in advising the President and senior government officials as to reasonable alternatives to the President's current plan of replacing old and diseased coffee bushes, as well as expanding the actual area planted.

Coffee and Conflict Resolution: The northwest of Uganda, as well as the north (Gulu), and some pockets along the border with the Congo (western Uganda), have been home to a number of militant guerilla groups. The UCDA began a coffee-planting program in Gulu during the 1997 season. Since then, 1600 hectares have been planted. Although there is concern that new areas not be planted to coffee (for fear of overproduction), it is certainly understandable and reasonable that areas that have suffered from civil unrest use coffee as a means of encouraging militants to put down the gun and pick up a hoe. The northwest has highlands that can produce very high quality coffee. These areas can be exploited for further coffee development in concert with conflict resolution activities.

3.0 Review of Coffee Competitiveness Strategies

The following narrative in Sections 3.1 - 3.6 discusses the coffee sector strategies that were agreed upon by the GOU, industry, and donors in the February 2002 President's Conference on

Competitiveness. Of the approximately 21 activities that were identified for implementation, about half have actually seen progress over the past 12 months.

The points outlined in Sections 3.1 - 3.6 provide a menu of activities that the coffee cluster has identified as critical areas that need to be addressed to alleviate constraints and increase competitiveness. It is not intended as a list of things to do for USAID; rather, the list provides a menu from which government, donors, and industry can select various activities that they feel they can competently address.

A discussion of each of the action areas follows:

3.1 Research Strategies

Develop New Genetic Materials: The Coffee Research Institute (CORI) has identified an Arabica genotype from Papua New Guinea (PNG) that can be grown at elevations as low as 1,200 meters. This genotype is resistant to coffee wilt disease and coffee leaf rust. This is an extremely important discovery, as the ability to grow in lower elevations and produce good yields, cup quality, and tolerate pathogens may allow this genotype to replace much of the area that is currently planted to wilt-affected Robusta. Currently, CORI has approximately 8 hectares of commercial test plots of the Arabica PNG genotype planted at 20 sites in Uganda. The EU is funding CORI research in this area. Every effort should be made to expand testing of the Arabica PNG and bulk up seedling numbers if positive findings result from continued testing.

Developing a wilt-resistant Robusta variety has been a priority of CORI; unfortunately, at this time, there is no strong Robusta candidate identified that is wilt-resistant, has good agronomics and cups well. Under the most optimistic scenario, if CORI discovered a wilt-resistant Robusta genotype today, the plant material would not be ready for commercial testing for another three years. This continues to be a significant bottleneck in Uganda's long-term plans to revitalize/replant its Robusta crop. There are serious questions that should be raised about the logic of replanting wilt-susceptible seedlings into geographies that have a high incidence of wilt. Fortunately, it appears that the Arabica PNG genotype may provide an alternative to replanting non-tolerant varieties at lower elevations. Nevertheless, it is likely that several more years will be needed before testing is completed, and seedlings are produced in sufficient numbers for mass distribution to growers.

Market Research & Promotion: The UCDA is able to gather, organize and analyze production, and export statistics efficiently. The organization, however, is weak when it comes to analyzing markets, trends, and competitors. There is a recognized need within the UCDA to develop more skills in market analysis, as well as product promotion. To date, there has been no activity within the UCDA to strengthen its market analysis and promotion skills. In part, this is due to budget limitations within the organization, as well as limited institutional knowledge in these subject areas.

Developing a Coffee Promotion Office in the EU

The EU imports 87% of all coffee shipped from Uganda. Much of this coffee (about 57% of total exports) enters the EU with no specific country of destination listed on its shipping documents. This makes it difficult to ascertain the specific structure of the EU market for Ugandan coffee exporters. Although volumes vary from year to year, the largest importers listed as receiving countries in official documents include Spain, Germany, Belgium, Italy and the UK.

The rationale for putting a Uganda coffee promotion office in London is driven by several factors. Using the Uganda House facilities at Trafalgar Square would reduce the overhead cost of the office by using non-utilized assets owned by the Ugandan Government. London is one of the major trading hubs in the EU, and because of this, would make a good location for a promotion office.

The scenario for start-up funding may entail a number of entities coming together to provide the necessary financial support. The Government of Uganda could contribute the office space (a non-cash contribution). EAFCA could be asked to contribute a token amount of funding in the beginning, increasing over time as sales increase. Donors would likely have to support some start-up costs, either through regional funding mechanisms, or country-specific funding mechanisms. A clear timetable would need to be developed to transfer funding away from the donors to EAFCA members or the GOU.

If the Ugandan Government is committed to the idea that it should be facilitating the promotion of its largest export, there are opportunities for them to partner with donors and industry. The Ugandan Government operates a consulate office in Uganda House in London at Trafalgar Square. Historically, the government has only occupied one floor of the facility and has rented out one floor. There are a total of five floors available; currently three floors are vacant. This office space can be used for a small promotional office located in a key capital city in Uganda's largest market[3]. In order to keep costs down, the promotion office could be set up in concert with (cost sharing with) other EAFCA member states or as a sole representative of Ugandan coffee. Ideally, the office would focus on both specialty and commodity coffees by employing a professional with solid experience in the European importing/roasting end of the business.

3.2 Production Strategies

Improving Coffee Plant Multiplication System: UCDA has focused a significant amount of budget resources toward increasing the production of planting materials produced in the coffee seedling nurseries. Industry sources report that nurseries are currently producing a large number (possibly 80% of capacity) of new planting materials. The new plants tend to have a large amount of variability in quality. There has been little effort to improve the quality of plant materials coming out of the nurseries, as producers have focused on volume rather than consistent quality.

Replant Wilt-Affected Plants with Resistant Genotypes: As mentioned in Section 3.1 (Research), no wilt-resistant Robusta genotype has been identified. Regardless, UCDA is moving ahead with their replant program. The plants that are currently in the nurseries will be provided to farmers at no cost by UCDA.

[3] In 2002, 87% of Ugandan coffee exports were shipped to the EU.

Expand Arabica Area Planted: The President's Conference on Competitiveness concluded that the area planted to Arabica should be expanded. The UCDA responded to this proposal by shifting more resources into Arabica production. As mentioned earlier in this report, the UCDA in 2003 is producing 70% Robusta seedlings and 30% Arabica seedlings. This is a shift from the former ratio of 85% Robusta and 15% Arabica.

Supporting the Development of Shade grown Coffee: There has been little active support for shade grown coffee at the field level, only supportive words for the concept within the industry and by government. In 2001, the COMPETE Project set out three shade grown demonstration plots in Jinja in coordination with the Eastern Coffee Farmers Association. The shade trees consisted of two varieties recommended by and purchased from ICRAF (Albizia chinensis and Grevillea robusta). The trees were planted into existing smallholder coffee plots. The demonstration plots were examined in January 2003, thirteen months after planting, and it appeared that there was approximately 70 - 75% survival rate of the shade trees.

Promises and Perception Issues Between SPEED and UCFA

There appear to be significant communication problems between SPEED and UCFA. In interviews with UCFA management, the consulting team was advised that SPEED was not delivering on promises it made to support UCFA in terms of training, organizational support and other matters. On the other hand, SPEED reports in its January - June 2002 Monitoring and Evaluation report that it provided an international consultant to UCFA to prepare planning and diagnostic documents, as well as staff training and strategic planning with Board members. If progress/capacity building is to be realized, the two organizations will need to improve communications and create a more harmonious working relationship.

Coffee Farmer Association Development: The Uganda Coffee Farmers Association (UCFA) is currently working with approximately 6,000 farmers in 30 registered associations. UCFA reports that they have an additional 30 organizations that may register as official associations in 2003, adding 4,000 additional farmers to the list of those involved in association development programs. According to UCFA management, the SPEED Project had agreed to work with the organization to build capacity; however, to date, management reports that they have not received training or other support promised by SPEED.

It appears that the SPEED Project prefers to work through other channels in their farmer association development activities, rather than trying to build capacity within UCFA. It is recognized that UCFA has weak management; however, in order to build sustainability, UCDA and donors may want to look for ways to reorganize UCFA in order to bring in stronger management that can carry the organization forward in the future.

Eastern Coffee Farmers Association (ECFA) is based in Jinja, and has 22,000 association members. It is one of the larger, if not the largest, coffee farmer associations in the country. To date, there has been little interaction with ECFA by existing projects. When the COMPETE Project closed, ACDI-VOCA agreed to undertake training and capacity building of ECFA's management; however, follow-up investigations indicate that this has not taken place. ECFA should be included as a partner in UTRADE, PRIME and APEP.

3.3 Processing and Value Addition Strategies

Assist Firms in Exploiting Value-Added Processing Opportunities: There has been little work done to assist firms in developing value-added coffee products or identifying channels through which these products can be moved to market. With the exception of the semi-washed Robusta mills purchased by the government and through private firms, there is little evidence that significant progress is being made in this area.

Support Expansion of Centralized Wet-Milling Faculties: Sixteen wet mills have been imported into the country in the last twelve months. Six of these mills were purchased by the GOU, and made available to rural farmer groups on a grant basis. The SPEED Project worked with UCDA to identify the grant recipients. To date, none of the grant recipients has installed the wet mills, as they do not have the necessary infrastructure in place to support the facility (i.e., the development of civil works and utilities has not been completed). It is unlikely that these facilities will be ready for the fly crop that will be harvested in the first half of 2003.

It is reported that one private firm (Kampala Domestic Stores) has set up one of the sixteen wet mills and operated the facility during the 2002 main crop period.

Monitoring and Reducing Mycotoxin Levels: Mycotoxin is a concern in the coffee industry worldwide. UCDA is well aware of the issues involved with high Mycotoxin levels in coffee. In mid-2002, UCDA joined with FAO and implemented a workshop on Mycotoxin control and monitoring. The issue of Mycotoxin in Uganda's coffee needs to be kept on the agenda, and farmers need to be educated on proper storage and drying techniques that can minimize the problem. No USAID program is currently focused on this area.

Increase the Availability of Short-Term Credit to SMEs: At the current time, there are no credit programs directly targeting coffee farmers. The GOU has a small credit program for small farmers, but this is reportedly being phased out. According to the EU-funded SUFFICE Project management, there is no model yet identified that can provide credit directly to small coffee farmers on a sustainable basis. SUFFICE provides credit and capacity building to micro-finance organizations, and they report a 98% debt recovery rate. When considering how to structure a credit facility for the coffee sector, the experience that SUFFICE has in this area will become invaluable.

SPEED is also working in the area of microfinance, leasing and loan guarantee activities. Much of their efforts to date have been on capacity building within the banking and microfinance sectors. This work could potentially benefit the coffee sector, assuming programs can be developed by private financial institutions that target or accept debt-financing activities of smallholders, SME's and input providers to the sector.

Providing credit to coffee sector SME's is of significant importance. If USAID is to have a positive impact in raising rural incomes, it needs to encourage the strengthening of existing

SME's, as well as the development of new ones. Examples of these firms include rural consolidators, millers, exporters, as well as input suppliers to the coffee sector. The challenges are significant. Historically, debt recovery has been a real problem in Uganda's production agriculture and agribusiness sectors. SME credit programs will need to take this into account, and create activities that are financially sustainable rather than repeating mistakes of the past. Prudence is the best path in developing future donor-funded credit activities. Donors should wait until they feel they have a viable model in place before implementing credit programs to the coffee sector, rather than developing models with a high probability of failure that can send the wrong messages to the industry.

3.4 Infrastructure Strategies

Improve Rural Infrastructure - Roads, Water, and Electricity: The GOU has ongoing programs for the development of infrastructure in rural areas. Unfortunately, the funds available are small, relative to the need. As mentioned above, the wet mills that were brought into the country under the UCDA program have not been installed, due (in part) to the lack of water and electricity infrastructure. In many cases, it may be logical to assume that future wet mill development will need to include budget line items for generators, as electricity in rural areas is either not available or inconsistent.

Cell-Phone Network and Market Information: Under COMPETE, it was demonstrated that market information could be quickly and efficiently delivered to rural communities via cell-phone network push technology. This technology allows for information such as price or volume to be downloaded into a text message, and then simultaneously sent to thousands of cell-phone numbers (service subscribers). In the coffee business, this technology could provide daily market reports to farmers and SMEs in rural areas. A second technology, "pull", would require that that subscriber dial into a specific number to download market information. In Uganda, wireless providers are ready to provide push or pull technology. At this point, however, no project or business has moved this technology forward. From the buyer's standpoint, this sort of transparency in the marketplace may pose a threat. Additionally, there is no central unbiased point through which a coffee discovery price can be identified within Uganda. The market information service would have to rely on buyers for a price quote, and this would tend to be prejudiced toward the lower price range rather than the mean. The Uganda coffee auction would provide a good transparent price discovery mechanism that could be used in this type of push/pull market information technology.

3.5 Market Strategies

The following section highlights a number of market strategies that can be employed to increase transparency, market share, unit value and profits within the coffee sector. These strategies were discussed by stakeholders and agreed on as the best path forward at the President's Conference on Competitiveness, February 2002 in Kampala.

The list of market strategies is not in order of priority. To effectively implement a number of these strategies, action needs to be taken in a well-coordinated progression. For example, the first step would be to improve coffee quality, develop coffee appellations and increase the amount of certified coffees (Utz Kapeh, organic, etc.).

At the same time, efforts to build business skill capacity of indigenous SME's and farmer organizations would need to take place. Closely following these activities, the coffee auction could be developed, along with an EU coffee promotion office. This type of approach addresses constraints in production, quality, market information, transparency, promotion, and market channels, resulting in higher revenues to farmers and agribusinesses.

Develop Coffee Appellations: The development of coffee appellations was initially introduced during the COMPETE Project. Currently, EAFCA is working with the USGS to develop pilot appellation sites in Ethiopia, Uganda and Rwanda. Funding delays have slowed the progress of this activity, though it is anticipated that by the end of 2003, the pilot appellation sites will be established.

Develop a Uganda Coffee Auction: The concept of a coffee auction was agreed upon at the President's Conference. The government promised that it would supply the facility (warehouse) in which the auction could operate. Originally, the government intended to lease the former Coffee Marketing Board warehouse on Port Bell Road in Kampala to the auction company for 1 USD/year for ten years. Before this deal could be signed, an international investor arrived and requested that the government provide a building for his apparel manufacturing operation. The building provided turned out to be the Port Bell Road facility. Following this, the government said it would find an alternative site for the auction, but never delivered on its promise.

The desire to move forward with the auction appears to be split along the line of local companies versus multinationals. Local firms and organizations appear to be very much in favor of developing an auction, whereas, the multinational exporters appear to be in opposition to this idea. Additional discussion of this issue is provided in the Annex of this document

Developing an EU Coffee Promotion Office: Although 87% of Uganda's coffee is exported to the EU, the government has yet to develop a promotional office in this strategic market. As mentioned earlier, there are opportunities for the GOU to provide office space within Uganda House at Trafalgar Square in London for this purpose.

Promotional Activities to Develop Name Recognition: Recognition of origin or name is important, particularly when targeting higher value markets. To date, no activity has taken place since the President's Conference to increase name recognition of Ugandan coffee in Europe (Uganda's main market); the GOU has entered into an agreement with the Chinese government to begin marketing Ugandan coffee in China. This joint venture has established two coffee shops in Beijing, and plans are in place for expansion.

Study Soluble Coffee Manufacturing & Marketing: In 2000 and 2001, there was interest by UCDA to examine the feasibility of developing a soluble coffee processing facility in Uganda. In 2002, a Ugandan private investor arranged with a Tanzanian soluble coffee plant to process Ugandan Robusta into instant coffee. This product is currently being produced and sold in Africa under a private label.

3.6 Regulations and Policy Strategies

Reorganize UCDA: The World Bank and Private Sector Foundation Uganda (PSFU) undertook a number of studies in 2002 and early 2003 to examine the structure of the UCDA. Following these ongoing activities, the UCDA has been paring down its labor force and streamlining its management. This is an ongoing process that will likely continue well into 2003.

Improve Security in Rural Border Areas: The GOU has budgeted increases for military spending. In part, this increase will be focused on reducing civil unrest in border areas. This will be a positive event for the coffee industry, as it will allow more coffee to flow from the Congo into Uganda for processing and export. Additionally, it will reduce the risk of purchasing product in the northwest and other areas that historically have been associated with security problems.

Develop Monitoring Systems for Certified Coffees: There are numerous coffee certification programs in use around the world (for example, Northwest Shade grown Alliance, Smithsonian Bird-Friendly, Certified Organic, Fair Trade, Rainforest Alliance - Eco OK, etc). The question is which system of certification is best for Uganda. DFID recently (in January 2003) entered into a contract with the Center for Development Research in Copenhagen, Denmark, to examine the costs and benefits associated with certification programs applicable to Ugandan coffee. It is expected that the results of this study will be ready in May 2003. The results should provide important information as to the direction that the industry should take in developing an approach to added value coffee production and marketing.

4.0 USAID SO7 Activities in the Coffee Sector

USAID Uganda has four projects that either directly target or overlap into the coffee sector. These projects include IDEA, SPEED, EAFCA and RATES, which support SO7.

4.1 Existing Project's Support to SO7

IDEA: IDEA works with small farmers in vanilla and cocoa production. These small farmers are often also involved in coffee production. Therefore, IDEA is positioned to support coffee sector activities through some of its existing client base.

SPEED: SPEED's involvement in the coffee sector follows the initial work on wet mill financial analysis that was performed under the COMPETE Project. SPEED has taken these initial findings and, together with UCDA, assisted in the selection process of grant recipients for semi-washing Robusta milling facilities. Following the awarding of these grants, SPEED's role has been to supply technical assistance to grant recipients. As none of the grant recipients has completed their basic civil works and utility installation for the semi-washed mills, there has been no direct TA provided by SPEED to the grantees for the start-up and operation training to run these facilities. Assuming that the grantees complete the civil works and utility installation in the first half of 2003, SPEED may be able to provide TA to these organizations for the November/December harvest period.

Coffee Sector Training in Brazil

In the second quarter of 2002, SPEED organized a trip to Brazil for a group of six new coffee mill managers, a UCDA official and the SPEED Coffee Coordinator. In Brazil, the group observed the operation of wet-milling equipment and took part in training in coffee quality improvement, mill management techniques and coffee handling.

SPEED signed a number of Memorandums of Understanding (MOU) with multinational coffee exporters operating in Uganda. The two firms involved are ESCO (Uganda) Ltd, and IBERO (Uganda) Ltd. ESCO is owned by a Swiss parent company and Neuman's of Germany owns IBERO. The Neuman Group is the second largest coffee trading company in the world. The MOUs signed between SPEED and the exporters outline SPEED's responsibilities in subsidizing the cost of extension agents to work with Ugandan coffee farmers. SPEED is also obligated to provide bicycles and motorcycles to the extension agents as part of their TA package.

The multinationals' obligation in the MOUs is to provide SPEED with information such as number of growers assisted, number of tons of coffee processed/purchased, and other process indicators.

SPEED - BDS Enterprise Linkage Approach

The SPEED Project was designed to deliver services to micro, small and medium-sized enterprises in Uganda. Specifically, the project focuses on improving access to financial services and business skill development. Additionally, SPEED works to strengthen the legal, regulatory and policy framework for the business-operating environment in Uganda. The project is active in both the agribusiness, as well as the non-agribusiness sectors. One of the key activities that SPEED focuses on is to work with the "Missing Middle". As defined by SPEED, this is the subset in the commercial finance sector that focuses on SME's, microfinance institutions, and commercial banks that lend to micro, small and medium-sized agribusinesses and non-agribusinesses. SPEED strives to deliver quality and demand-driven services/training to the "Missing Middle".

SPEED was not designed as a coffee-specific activity, but is currently involved in the coffee sector on an interim basis at the request of USAID. The project is working with a number of multinational coffee exporters to improve coffee quality and raise farmgate incomes. The improvements in coffee quality will increase the gross sales value of the coffee for the exporters, and it is anticipated that the increase in price received by exporters will be passed along to the farmers.

Farmers are in a weak negotiating position when it comes to selling their coffee to local or multinational buyers. From the farmer's perspective, the marketplace is not transparent. The farmer is also selling into a fairly concentrated market, with a near monopsonistic market structure. Over time, market concentration has increased. This increase in market concentration has been exacerbated by low coffee prices that have driven weaker firms out of the business. This has diminished competition in the sector.

SPEED can play a constructive role in continued support of its large multinational partners, as well as working with indigenous SME companies to develop activities that improve coffee quality. In addition to its work with the commercial side of the industry, SPEED also needs to ensure that farmer interests are clearly represented in their approach. To do this, SPEED can work with its commercial partners and farmers to develop sales contracts that clearly link price and quality. This will benefit both buyers and sellers, as it will demonstrate to farmers that improving quality can raise farmgate incomes. The transparency issue may be best addressed under UTRADE or APEP, as it may require a longer-term and more comprehensive set of activities than SPEED can deliver to the coffee sector. Nevertheless, wherever possible, SPEED should strive to improve transparency, particularly at the farmgate. Without improvements in transparency, it is unlikely that USAID will achieve its targets of reducing rural poverty and hunger in Uganda.

The goal of this relationship is to increase coffee quality and price paid to the farmer. This is an important and admirable objective; however, there is no linkage of quality improvements to price mentioned in the MOU that was read in the course of preparing this document. In the future, USAID programs should negotiate MOUs that clearly state that when objectively verifiable increases in quality are established at the farmgate, there will be a corresponding increase paid to the growers for their coffee. This price incentive (quality bonus) can be linked to the London or New York coffee price. For example, an X% increase in quality measured by percent moisture under a base level, screen size over a base level, reduction in trash and extraneous matter under a base level, will result in a price premium paid to the farmer. This price should be calculated in advance and shown to the farmer at the beginning of harvest. These types of transparent systems are commonly used when buying horticultural products in developed countries, and these same contractual agreements can be developed for the Uganda coffee sector. In cases where coffee buyers plan to wet mill the product, a formula for rewarding for cherry quality will need to be worked out. Again, this can be based on a transparent price for a given quality.

It should be pointed out that SPEED was never intended to be the Mission's primary vehicle for assistance to the Ugandan coffee sector. It is fulfilling an unexpected interim need at the request of the Mission.

EAFCA: Eastern African Fine Coffee Association (EAFCA) - as the name implies, this organization is focused on the fine coffee sector. The USAID-funded activity works to increase coffee farmer incomes, improve quality, develop market transparency, and promote East African specialty coffees around the world. The project accomplishes this by supporting a number of activities, including, but not limited to, appellation development, coffee auctions, coffee certification programs, and domestic, as well as international coffee promotion activities. EAFCA works in six East African countries, including Ethiopia, Kenya, Uganda, Tanzania, Rwanda, and Burundi. EAFCA is funded under REDSO through the Global Development Alliance out of Washington D.C. The EAFCA project was not specifically designed to address USAID Uganda SO7, but economic outcomes as a result of EAFCA's work supports the Mission's SO7 objectives.

RATES: Regional Agricultural Trade Expansion Support program was started in 2002, after the award of the implementation contract to Chemonics International. The project is headquartered in Nairobi, Kenya; however, a full-time staff member responsible for coffee trade development has been assigned to the EAFCA headquarters in Kampala[4]. RATES' overall objective is to increase the trade of East African coffee in domestic, regional, and international markets.

[4] The RATES representative was out of the country and unavailable during the preparation of this report; therefore, no interview with a RATES representative was conducted.

4.2 Additional Opportunities to Support SO7 by Existing Projects

IDEA: The IDEA Project is well positioned to act as a precursor to upcoming investments in PRIME and APEP. There are a number of activities that IDEA can undertake that will support these future investments and lead to a more rapid start-up of the new projects.

> **Pheromones and Mycopesticides For Control of Cocoa Capsids: Research in Ghana**
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> Cocoa is the main export crop of Ghana, maintaining directly or indirectly the livelihoods of over six million people. Capsids are the most important insect pests, causing losses estimated at 100,000 tons or 25% of the crop. Currently, conventional insecticides provide the only effective methods of control, but farmers rarely use recommended spray programs because of expense and difficulty of application. A USAID-funded research project aims to develop an effective mycoinsecticide against the two main species of cocoa capsids in Ghana and to identify the sex pheromones of these capsid species. These project outputs will make possible evaluation of new approaches to monitoring and control of cocoa capsids that are appropriate for use in Ghana and environmentally acceptable.
>
> This project was supported by DFID (prior to 2002) and will be continued with funding from the USAID Sustainable Tree Crops Program and from the Cocoa Industry.

Cocoa is an important alternative crop in the higher rainfall coffee production areas. IDEA has experience in the cocoa sector through its support of the Uganda Cocoa Association. The IDEA Project should continue with its activities in the cocoa sector, focusing work on the training of extension agents and the creation of demonstration plots, improving quality of cocoa beans, and improving the genetic material. Cocoa is not applicable to all areas of Uganda, but in geographies where climatic conditions allow, IDEA can promote cocoa as a crop to be incorporated into a coffee/cocoa/ vanilla farming system. This farming mix will diversify farm income and therefore, reduce the financial risk of crop loss or income loss due to price variations. This type of farming mix is also environmentally sound, as it promotes the production of permanent crops that are beneficial in terms of soil conservation, biodiversity, and habitat maintenance. Capsids and primates are the primary pests of cocoa farmers in Uganda. DFID and USAID have supported research in capsid control in cocoa in Ghana. The findings of this research should be considered for application in Uganda. If pheromone control of capsids in cocoa is possible, this will provide an environmentally sound, easy to apply system of controlling this pest. The outstanding question for the pheromone system will be its cost to the farmer and efficacy.

Many extension techniques to improve the quality of coffee can also be employed to improve the quality of cocoa. For example, both crops should be grown under shade, and dried on tarps or papyrus mats (kept off the ground). Farmers need to be trained in proper sun-drying methods and storage. Local consolidators who buy coffee from farmers can also buy cocoa. The lessons learned in coffee inspections prior to export can also be applied to the cocoa industry to improve export quality and assist in the long-term development of Uganda as a quality producer of cocoa. At the current time, cocoa is not inspected (graded) prior to export.

IDEA has a long history of working with vanilla farmers in Uganda. This work also dovetails well with the coffee sector in that vanilla and coffee (as well as cocoa) perform best when produced under a shade tree canopy. As with cocoa, vanilla may not be applicable to all geographies in which Ugandan coffee is produced; however, in areas that support production of vanilla, it should be encouraged as a companion crop to shade grown coffee.

Given the importance of shade systems for coffee, cocoa and vanilla, IDEA can work with ICRAF and other organizations to develop shade grown coffee/cocoa/vanilla demonstration plots throughout Uganda. Additionally, IDEA can work with UCDA and its coffee seedling producers to multiply shade trees that can be distributed with coffee seedlings. IDEA's expertise in horticultural production can also be used by coffee nursery operators to improve the genetics, quality, and consistency of plant materials being produced in the nurseries.

SPEED: SPEED should continue its work to develop extension programs with the multinational exporters. This will be a relatively easy and straightforward task, as the partner companies are well organized, technically competent, and well funded. In addition to continuing its extension programs with multinationals, it should also look for ways to provide similar services to locally owned and operated companies. Unlike the multinationals, the local firms often lack the organizational structure, skills, home office support and financial stability that the multinationals enjoy. Nevertheless, if significant progress is to be made on SO7 (reducing rural poverty), effective programs need to be designed that target local companies and create mechanisms by which profits from these firms are plowed back into the community, rather than retained in off-shore accounts by parent companies.

A second area that should be examined is the benefit of developing mills for fully washed coffee and/or semi-washed coffee. In the 1960's, Uganda produced 40,000 tons of fully washed Robusta annually. When the coffee sector was nationalized, the washing mills (located in rural areas around Uganda) went out of business. Today, there is an attempt to revitalize the washed coffee subsector; but rather than using the fully washed system, SPEED and UCDA have opted to use a semi-washed system. The questions that need to be considered when using the semi-washed system include: is this an applicable system for Uganda (given that semi-washed coffee processing facilities have more moving parts and are more difficult to maintain than well-designed fully washed systems)? Secondly, the semi-washed system does not provide a fermentation stage, as does the fully washed protocol. Cup quality using fully washed systems, is considered superior to semi-washed systems. Given the fact that cup quality is correlated to price, it would be advisable to explore the development of more fully washed systems, rather than promoting semi-washed.

Under the SPEED/UCDA program, coffee dryers were purchased, and will be set up at the semi-washed mills. Throughout East Africa, coffee is sun-dried. The question of mechanical drying (with its high fuel costs, as well as maintenance and fixed capital costs) needs to be examined before additional monies are invested in this technology. An alternative to purchasing mechanical drying systems is simply to have a local coffee production association construct drying tables or a well-drained concrete slab on which their coffee can be dried. This requires no moving parts, and relies on human labor and solar energy rather than fossil fuels to dry the coffee.

Everyone within the coffee sector agrees that it is important to improve quality at every level of the industry. This has been reiterated at numerous workshops, industry meetings and at the farm level. The question that needs to be raised is not if quality needs to be improved, but how. Providing better semi and fully washed products is just one way of improving quality. Other quality increases will come with improved sun-drying methods, appellation development, and better product differentiation, as well as improved linkage mechanisms between quality and price.

To fully implement a number of these quality improvement programs, farmers, millers and consolidators will need to make significant investments in fixed capital and operating capital. Management skills and credit-worthiness are well-recognized constraints within Uganda's micro and SME business sectors. SPEED is addressing the "Missing Middle" under its current BDS Enterprise Linkage program approach. To strengthen management skills and credit-worthiness, SPEED should continue its activity in this area, and USAID should continue coffee sector business strengthening activities under UTRADE, APEP and PRIME.

East African Fine Coffee Association Strategic Objectives

Paraphrased from EAFCA's Board of Directors Strategic Plan - Coffee Years 2002-2005

- Improve financial stability & productivity of the Association
- Improve the welfare of small-holder coffee farmers
- Improve coffee quality in the fine coffee sector
- Provide education & training to specialty coffee farmers in East Africa
- Develop auctions & regional market infrastructure
- Work to unify the regional industry
- Liaison with organizations and institutions on matters relating to regional fine coffee promotion
- Establish an African-based certification body and work with others to develop globally accepted certification programs.
- Promote consumption in domestic and international markets

There is a need in Uganda to update the Agricultural Seed and Plant Statute of 1994. Some work in this area has recently been done. A new draft Seed and Plant Statute was released in January 2003 (at the time this report was being prepared). Given SPEED's legal department, the project is well placed to review the draft statute and make comments to donors and government as to its strengths and weaknesses. This is particularly important to the coffee sector in that the government has identified the need to replant old and wilt-affected bushes. To do this most efficiently, it may be necessary to move genetic material outside of the country for multiplication, then re-import it in tissue culture form (plantlets). This prospect has run into some resistance with government, and the regulations governing the movement of plant materials in and out of the country need to be clarified.

EAFCA: EAFCA can play an important role in preparing the sector for additional USAID investments. Many of EAFCA's objectives are parallel to the objectives that are likely to be developed under UTRADE, PRIME and APEP.

Sustainable development requires a three-legged stool approach in its strategic plan. It must be economically viable, socially viable, and environmentally sound. If any of these basic components are weak, the success of a sustainable development program is in jeopardy.

EAFCA can work on strengthening the support structures for a sustainable coffee sector in several areas. The organization has identified the development of auctions and appellations as part of its operating plan. By moving ahead in these areas, as well as continuing their work in price risk management (in association with the World Bank and Union Export Services Ltd), EAFCA will provide the foundation to developing a sustainable coffee sector that contributes to poverty alleviation. EAFCA should also continue efforts to identify certification programs that will assist farmers in maximizing incomes. Certification programs such as shade grown, bird-friendly, organic, etc., are relatively new concepts to Uganda. Much work needs to be done in this area in Uganda with producers and exporters. This said, an equal amount of work needs to be done at the consumer end. EAFCA can play a role in identifying partners in Europe, Asia, and North America that can collaborate with them in educating consumers as to the environmental benefits of buying certified Ugandan coffees. This will be a long and expensive process, but the benefits of a well-executed certification program are well worth the costs.

EAFCA has a unique role in the region in that it can develop value addition models in various member countries, evaluate these models, then replicate them where applicable throughout East Africa. This provides an efficient way of moving knowledge and skills within the region to exploit market opportunities.

One of the weaknesses that EAFCA faces is staffing. Outside of its headquarters in Kampala, there are no full-time EAFCA managers in member countries. All of the EAFCA staff located in member countries hold down primary jobs within the coffee industry and work on EAFCA issues in their spare time. The challenge for the organization over the long run will be how it can develop a sustainable cash flow adequate enough to employ full time staff in each member country.

RATES: RATES is currently closely linked with EAFCA. The RATES manager in charge of coffee sits in the EAFCA office in Kampala. This provides an efficient mechanism to link these two activities.

Given that RATES has a regional focus, it is appropriate that it addresses issues that affect the broader East African coffee industry. Quality is an ongoing theme, and RATES can focus on this issue through work in mycotoxin monitoring and reduction activities, as well as standardization of quality measurements throughout the region. The coffee industry does not have an accepted set of international quality standards that relate to specific grades. Throughout the world, coffee is measured in similar ways (moisture content, size, percent broken, etc.), but specific grades from country to country often allow different amounts of variables. RATES has the opportunity to develop a standardized quality formula within East Africa. This would help harmonize the market and make it easier for international buyers to evaluate products from this region.

5.0 Supporting Public-Private Dialogue Between the Coffee Cluster and GOU

5.1 Public-Private Dialogue: Opportunities in Transition Activities

There are a number of opportunities for the GOU and the coffee cluster to engage in constructive dialogue.

Carbon Credits: In the area of shade grown coffee, Uganda's Department of Forestry has shown initiative in its efforts to examine opportunities to attract carbon credits (under the Kyoto Protocol) to Uganda. The UCDA and USAID can work together in concert with the Department of Forestry to pursue carbon credits for the coffee sector.

Currently, the Kyoto Protocol does not provide a specific mechanism for payment to coffee farmers for planting shade grown coffee and receiving compensation for removing carbon from the atmosphere. When the Kyoto Protocol is renegotiated in 2006, a proposal to include a provision for compensation for planting forests (and shade trees) may be included. At present, a number of coffee associations have reportedly been able to receive compensation under the current version of the Kyoto Protocol. The government, in concert with the coffee cluster, should examine these cases to identify mechanisms by which Ugandan coffee farmers can benefit from carbon credits.

One important hurdle that the government will need to address under Kyoto is that the carbon removed from the atmosphere must be locked up in perpetuity. This may prevent farmers from cutting down shade trees to use for firewood or lumber. A certification and inspection system also needs to be created in Uganda to ensure compliance.

Government Support of Market Development Activities: There are a number of opportunities for the GOU to support the coffee cluster by contributing non-performing or under-performing assets. As discussed earlier in this document, the GOU has office space available in Trafalgar Square in London that is not occupied and can be used for a coffee promotion office. In addition, the government has promised to provide a warehouse for auction facilities, but as yet, has not delivered on this promise.

5.2 GOU's Political Will to Implement Sector Strategies

There is strong political will at the highest levels of government to reduce poverty and strengthen the coffee sector. This political will does not always translate into action at the management level of government, as competing special interest groups sometimes interfere with implementation or the policy makers in the government do not clearly identify what and how they want tasks accomplished.

The coffee sector is politically significant, as it impacts many political constituents. Politicians are tempted to use give-away programs and other subsidies to win political favor of voters. This is as common in Uganda as it is in Iowa. Donors just need to be aware of the political realities and choose their battles wisely. In many cases, donors can influence political decisions by helping politicians identify alternatives to those that may have negative effects within the coffee cluster. Case in point is the President's plan to expand coffee production at a time when the world coffee market is flooded. Donors can help the President by providing His Excellency with alternatives, such as a combined coffee/cocoa/vanilla expansion program that will diversify incomes at the farm level and reduce the amount of coffee delivered to the international market.

5.3 The Private Sector's Buy-in of Sector Strategies

In general, there is good private sector buy-in on the strategic activities that were put forward at the President's Conference on Competitiveness in February 2002; however, on certain issues, there is a difference of opinion between coffee sector multinational corporations and local companies.

This difference of opinion can be exemplified by examining who supports the proposed coffee auction and why. When the auction was proposed, the multinationals appeared to be slightly negative to somewhat indifferent about the prospects of having an auction. These large trading companies prefer a status-quo laissez-faire business environment, where they are free to purchase bulk coffee in the field at the lowest possible price, add the value by milling coffee at their Kampala-based facilities, and export the final products.

Smart Card to Improve Record Keeping at Jamaica's Coffee Industry Board

The USAID/ Carana Corp. New Economy Project (NEP) is assisting Jamaica's Coffee Industry Board, Commercial Division, to improve their data capture processes at coffee depots in the Blue Mountain Area. Over 6,000 Jamaica Blue Mountain ™ coffee farmers will be issued a "Smart Card" (registration card) that from early 2003, will be scanned to record the delivery of coffee at the five major depots, using wireless data capture devices. This will significantly improve the existing payment system for farmers by improving the quality of data captured, thereby speeding up payments and reducing the incidence of coffee stolen from genuine farmers being bought from unregistered vendors.

In Uganda, a similar Smart Card system can be used by UCDA in the management of coffee appellations. This system will assist in reducing fraud and provide an accurate system for tracking quality and volume for individual farmer and the appellation as a whole.

The smaller local firms support the auction; as they see it, it plays to their strengths. Small local firms are good at purchasing raw product, milling and preparing product for export. They are not particularly good at export marketing and they are very weak in understanding, developing and using market risk management tools, such as hedging in coffee future markets. Because of this weakness, local exporters have suffered significant losses in the recent market downturn. The auction allows the local companies to procure the raw coffee, add the value locally and sell it locally. The importer takes the market risk once the coffee leaves Kampala - not the local company.

Any activity that is viewed by the multinationals as competing with their need to maximize volume will be viewed suspiciously. The multinationals operate on very slim margins. They will feel threatened if they think that their product base is eroding by donor attempts to work with local companies to add value and differentiate product and create new market channels.

A second discord in the industry is at the roaster level. It is in the best interest of Ugandan coffee producers to develop the

Uganda name as a recognized origin. Columbia has done an excellent job with its origin promotion program, and this has paid off handsomely for the country's growers. Roasters (and many of their suppliers), for the most part, do not want consumers to know the origin of their coffee, as it reduces their flexibility in blending the cheapest coffees available to achieve their final product. This is simply the nature of the industry. As Uganda develops programs to increase its recognition at the consumer level, undoubtedly, there will be voices within the commodity sector that view this as a threat and will oppose it.

6.0 Findings & Recommendations

6.1 Conclusion

The Government of Uganda and industry continue their support of the strategic activities that were agreed upon at the President's Conference on Competitiveness in Kampala (February 2002). There has been progress on approximately half of the activities that were identified by the coffee cluster as relevant to the development of the sector.

Although the coffee cluster is in general agreement on what it wants to accomplish over the next five years, there is still discussion on how certain activities should proceed, and what level of priority various activities should be allotted. A few of these key activities still subject to discussion include:

- It is agreed within the coffee cluster that Uganda's coffee population is old and suffers from a high incidence of disease. The crop needs to be replaced. The key question is how much of the crop should be replaced, given the fact that the new clonal varieties of Robusta yield twice as much per hectare as the old traditional varieties. A second aspect of the replant question that is being discussed is how much of the crop should be replanted as Arabica, and how much Robusta. On this issue, the UCDA appears to be proposing a 70%:30% Robusta - Arabica replant program. This is an improvement over the existing ratio of Robusta to Arabica, currently estimated to be 85%:15%.

- Coffee wilt is killing approximately 5% of Uganda's Robusta plant population annually. There is no resistant variety on the immediate horizon, and researchers are most likely five to seven years away from even identifying candidates for commercial trials. Given this fact, some people are debating the wisdom of spending money on a large-scale replanting program for Robusta when the new plants will be susceptible to the coffee wilt. CORI has identified Arabica PNG that can be grown at low elevations, and is resistant to wilt. This may be a good candidate as a Robusta replacement in geographies that suffer from high incidence of wilt. The problem at this point is the Arabica PNG genotype is only at a preliminary commercial trial stage. It will take several years before adequate numbers of this plant can be multiplied under conventional production techniques.

- Given the need to rapidly multiply coffee plants, the GOU needs to examine the regulatory environment for the import and export of genetic material. The government and industry are currently at odds over the importation of plantlets developed from Ugandan clonal genetic material. This issue needs to be resolved so that current private sector projects can move ahead, and future activities such as the rapid multiplication of Arabica PNG can be augmented by offshore tissue culture labs.

6.2 Recommended Transitional Activities Actions

The existing projects (IDEA, SPEED, EAFCA and RATES) are well positioned to play an important precursor role in transitional activities leading up to the implementation of UTRADE, PRIME, and APEP.

IDEA Transitional Activities: There are opportunities for the IDEA Project to build on its past work in the cocoa sector as a means of supporting the coffee cluster. In particular, IDEA can work with coffee farmers who are located in geographies with a high incidence of coffee wilt and provide TA on cocoa production, plant multiplication, pest management, and optimizing shade cover for the cocoa crop.
Shade is required for cocoa production, and provides benefits for coffee production. IDEA can work with ICRAF and coffee nurseries around Uganda to produce and distribute shade tree seedlings for both cocoa and coffee producers. IDEA can use its experience in providing demonstration plots in low value crops to develop models for shade grown coffee demonstration plots. This would be a valuable precursor to both PRIME and APEP.

Given IDEA's expertise in horticultural production, there may be opportunities for the project to support UCDA and the coffee nurseries to improve the quality of nursery stock and assist in the development of a nursery quality assurance program. This work would benefit the coffee growers by ensuring that they receive high quality plant materials.

Capsids and primates are the primary pests for cocoa producers in Uganda. USAID has funded research in Ghana on using pheromones and other biological systems to control capsids. IDEA can work with the USAID Sustainable Tree Crop project that funded the capsids work to determine if the findings identified in Ghana are applicable to Uganda. Additionally, IDEA can examine and demonstrate farming systems that help control primate pests. One strategy already used in Uganda is to plant bananas around cocoa. Monkeys prefer bananas to cocoa, and therefore the bananas are eaten, rather than the cocoa crop. IDEA can work with cocoa farmers to determine if this is a viable mitigation strategy, and determine the best cropping pattern (spatially and seasonally) to minimize primate damage in cocoa.

IDEA has also worked with vanilla producers in Uganda. Vanilla requires shade, and can be inter-cropped with shade grown coffee and cocoa. By including vanilla into the shade grown farming system crop mix, USAID can promote projects that diversify farm household incomes and help mitigate financial risk associated with ever changing commodity prices. From an environmental aspect, Uganda benefits as shade grown systems for these crops encourage biodiversity, as well as natural resource conservation. Shade grown farming systems also provide additional opportunities for income generation through the sale of logs, lumber, honey, and other forest products.

Cardamom has also been identified as a potential crop for farmers to diversify their income within Robusta growing areas (particularly the Jinja district). During the transition period, IDEA can examine the opportunities in cardamom production and provide these findings to the APEP project once implementation has begun.

SPEED Transitional Activities: SPEED should continue its work with the multinational coffee exporters to develop extension systems that deliver higher quality coffee to the buyers, and correspondingly higher revenues to the growers. SPEED needs to develop a formula with its multinational partners that transparently shows the relationship between quality improvements and financial benefits to farmers.

As SPEED learns from its work with the multinationals, it needs to adapt these lessons to develop extension models that are applicable for local coffee buying, milling, and exporting companies. Finally, SPEED needs to develop a third model for extension work that can be used with farmer associations. This model needs to deliver information to growers so that they understand how to and can benefit from the production of quality coffee.

SPEED also needs to redouble its efforts with its partners in the development of the semi-washed Robusta milling facilities. All of the hardware is currently in the country; however, only one wet mill has been constructed. SPEED needs to assist its partners in developing the civil works and infrastructure before the start of the next coffee harvest season in late 2003. This may take highly focused efforts by SPEED to identify the bottlenecks that are keeping its clients from installing the hardware, as well as developing focus programs to ensure that the processing facilities are operated/managed in an efficient manner.

Work also needs to be done that compares the costs and benefits of developing additional semi-washed facilities versus fully washed coffee-milling operations. SPEED can facilitate this research by examining operation management issues, capital costs, variable costs, and final product quality and market opportunities for fully washed and semi-washed products.

On legal and regulatory issues, SPEED can use its in-house attorneys to review the most recent version of the Agricultural Seed and Plant Statutes. The new draft regulations have recently been released by the GOU, and these regulations will have direct impact on the coffee sector. The government needs to get these regulations right in order to facilitate its plans to improve the quality and volume of genetic material available to the sector.

EAFCA Transitional Activities: EAFCA can support investments in UTRADE, PRIME, and APEP by continuing its work in appellations, auctions, certification programs, and product promotion.

DFID is currently working on a market study report that will examine the marginal benefits of various certification programs. Once this report is out, EAFCA can develop a regional strategy that focuses resources on certification programs that yield the highest return to rural households. EAFCA can also work to identify partners in consumer countries that will work in concert with East African coffee producers to promote coffees that fall under these certification programs.

6.3 UTRADE, PRIME and APEP Coffee Sector Activities

To maximize the benefit of future USAID investments in Uganda's coffee sector, efforts need to be made to integrate the activities between these projects (UTRADE, PRIME, and APEP) so that the synergies are maximized.

The following are examples of activities that should be considered for inclusion in the coffee cluster under UTRADE, PRIME, and APEP.

UTRADE

- In concert with UCTF, EAFCA, and UCDA grow Uganda's specialty coffee market
- Work to develop a Uganda Arabica Coffee Auction
- Form an alliance with EU, Asian, and North American promotional partners to develop specialty coffee market
- Develop Uganda as a consumer recognized origin
- With GOU, open a coffee promotion/ market intelligence/ commercial representative office in the EU (the office maybe jointly funded by EAFCA member states)
- Work with farmer organizations and SMEs to create new products (washed coffees, appellations, etc.) & new market channels for local firms
- Provide market risk management training to local SMEs and exporters
- Provide business skills training to millers & exporter SMEs
- Work with wireless phone network providers to develop text messaging system for market information
- Develop export quality standards for cocoa & vanilla
- Link with PRIME, APEP, and local SMEs to consolidate volume and develop market channels for appellation and other specialty coffees
- Develop a venture capital and/or grant facility that could be used by local and international business to invest in technologies and systems that improve coffee quality, develop markets, and promote Ugandan coffee
- Work with RATES to develop harmonized East African coffee quality standards

PRIME

- Develop Shade Grown Coffee (SGC)
- Research, demonstrate, and develop a shade grown coffee/cocoa/ vanilla farming system to minimize risk and maximize grower incomes
- Promote coffee/cocoa/vanilla farming as buffer to national parks and other environmentally sensitive areas
- Using SGC, develop "islands of habitat" in areas where coffee culture is the dominant culture/ land use (increase biodiversity)
- Work at the farmer level to develop "certified" coffee production link to UTRADE clients for marketing
- Expand coffee/cocoa/vanilla farming models in areas at environmental risk due to high slopes or other factors
- Work with UCDA in west, northwest, and northern Uganda to link coffee development activities with conflict resolution (swords to plows)

- Work with GOU Forestry Department to explore opportunities in SGC and carbon credits
- Work with EU/US/Asian partners to promote coffee/cocoa/vanilla which advance biodiversity and sound environmental production practices (Smithsonian & RSPB)
- Work closely with UTRADE and PRIME to develop quality, volume, and market for specialty coffees

APEP

- Develop farmer organization linked to multinational exporters and locally owned SMEs
- Deliver production TA (improve yield, handling and quality)
- Develop coffee appellation and introduce "Smart Card" technology to track production and reduce fraud
- Provide TA and training to semi and fully washed coffee millers
- Applied research on developing a capsids IMP program in cocoa
- Provide business skills training to farmers and sector SMEs in rural areas.
- Build capacity in shade tree/coffee/cocoa/ vanilla nurseries (improve,
- Quality, consistency and volume)
- Provide funding to Masters level students to study biotechnology in the US (research on coffee, cocoa and/or vanilla)
- Continue regulatory reform work in plant material, quality regulations, and other policy matters
- Train coffee growers in cup quality via district training and seasonal cupping competitions

ANNEX A List of People and Organizations Interviewed

Name	Organization	Contact Address
Paul Mugambwa	Farmer/ Exporter / Chairman, UCDA	077-700905
Dr Georgina Hakiza	Coffee Research Institute (CORI)	jjhakiza@imul.com
Pascal Musoli	Coffee Research Institute (CORI)	cori@africaonline.co.ug
Patrick Kucel	Coffee Research Institute (CORI)	cori@africaonline.co.ug
Fred Kawuma	EAFCA	fkawuma@EAFCA.org
Robert Nsibirwa	EAFCA	secretariat@EACA.org
Robert Gensi	ACDI/VOCA,	voca@imul.com
Stanley Marenge	ACDI/VOCA SCOPE Project	smarenge@EAFCA.org
Fred Nyonyintono	Eastern Coffee Farmers Association	077-313892
Moses N. Kintu	Eastern Coffee Farmers Association	077-075626349
Solomon Rutega	GOU/China Coffee Promotion Project	solorut@yahoo.com
Clive Drew	IDEA Project	clive-adc@starcom.co.ug
Martin Fowler	Ministry of Agriculture &Fisheries	mfowler@utlonline.co.ug
Samuel Iga Zinunula	National Small Business Center	nsbc@utlonline.co.ug
Dr. Peter Ngategize	Plan for Modernization	planmode@infocom.co.ug
Nimrod Waniala	Private Sector Foundation (PSF)	077-221448
Gideon Badagawa	Private Sector Foundation (PSF)	077-601646
Jack Thomson	SPEED Project	041-346849
Ralph Chaffee	SPEED Project	rchaffee@speeduganda.org
J. Ledgewood	SPEED Project (Micro finance)	041-346864
Andrew Falconer	Exporter / KAWACOM (U) Ltd	260-200
Henry Ngabirano	UCDA	henga@infocom.co.ug
Joseph Nkandu	UCDA	077-595030
John Byarugaba	Uganda Coffee Trade Federation	077-466 366
Phil Bettes	Exporter / ESCO	245-162
Greg Stough	IBERO (U) Ltd.	077-200-462
David Barry	Exporter/ HSBC Equator Bank	256-41250696
Lene Hansen	SUFFICE / EU	077-404273
Henry Mutabazi	SUFFICE / EU	077-404273
Charles Karamagi	Exporter / Intertrade Services / UCTF	acme@starcom.co.ug
Daniel Ddamulira	USAID	dddamulira@usaid.gov
Randolph Harris	USAID	rharris@usaid.gov
Jeff Levine	USAID	jlevine@usaid.gov
Paul Crawford	USAID	pcrwaford@usaid.gov
Greg Booth	USAID	gbooth@usaid.gov
Walter Welz	USAID	wwelz@usaid.gov
David Mutazindwa	USAID	dmutazindwa@usaid.gov
Diana Atungire	USAID	datungire@usaid.gov

ANNEX B List of Relevant Documents Reviewed

- Annual Reports for 1999/2000 and 2000/2001
  Uganda Coffee Development Authority
- UCDA Monthly Report for December 2002
  Uganda Coffee Development Authority
- Annual Reports for 2001/2002
  EAFCA
- Board of Directors Strategic Plan Coffee Years 2002 – 2005
  EAFCA, September 2002
- Coffee Certification In Uganda: Feasibility Study TOR
  Department for International Development (DFID UK)
- Recommendations for Technical Assistance to the Cocoa Industry
  IDEA Project 1996
- Leasing for Agriculture
  Trends and Issues in Micro-Finance-Informal Information Exchange Meeting, Presentation Paper October 2002
- The Ugandan Coffee Strategy 2002
  Private Sector Foundation
- Enhancing Coffee Sector Competitiveness: Realigning the Institutional Structure, Supervisory and Regulatory Functions
  Private Sector Foundation
- Coffee Markets in East Africa: Local Responses to Global Challenges or Global Responses to Local Challenges
  S. Ponte, Center for Development Research, Copenhagen, Denmark
- Agricultural Finance; Presentation and Explanatory Text
  GTZ, Financial Systems Development Program
- SUFFICE Program Summary
  Support to Financial Institutions and Capacity-Building Efforts in Uganda
- Economic Growth and Transformation Strategy
- Paper presented to the meeting of The Consultative Group For Uganda Prepared by the Government of Uganda, Development Partners and the Private Sector, MAY 2001.Strategic Exports in Uganda: Performance and
- Growth Prospects Synthesis Report
  Commissioned by: European Union, United Nations Development Program, U.S. Agency for International Development, U.K. Department for International Development, and World Bank.
- UGANDA COMPETES: Uganda Competitive Private Enterprise and Trade Expansion Project (COMPETE), final Report
  CARANA Corp. May 2002
- Selected Reading of EU Project Evaluation in the Ugandan Coffee Sector:
  Annex 1a: Evaluation of Previous EU-Funded Coffee Research
  Annex 1b: Evaluation of Previous EU-Funded Coffee Research
  Annex 1c: Review of the Medium Term Plan for EU Support to Coffee Research
  Annex 1d: Effective Research Services for Sustainable Coffee Production in
  Annex 1e: Economic Justification: Coffee Wilt Disease Research
  Uganda: A Project Proposal to the EU

ANNEX C Ugandan Coffee Sector Trends

Coffee Price and Volume Trends: The following section (Annex C) examines key historical data from Uganda's coffee sector. Figure 2 (below) shows export volumes in millions of bags and export earnings in hundreds of millions of USD. As can be noted from the volume trend line, over the past 22 years, Uganda has increased its production volume by about 30%, going from exports of approximately 2 million bags in 1980 to just over 3 million bags in 2002.

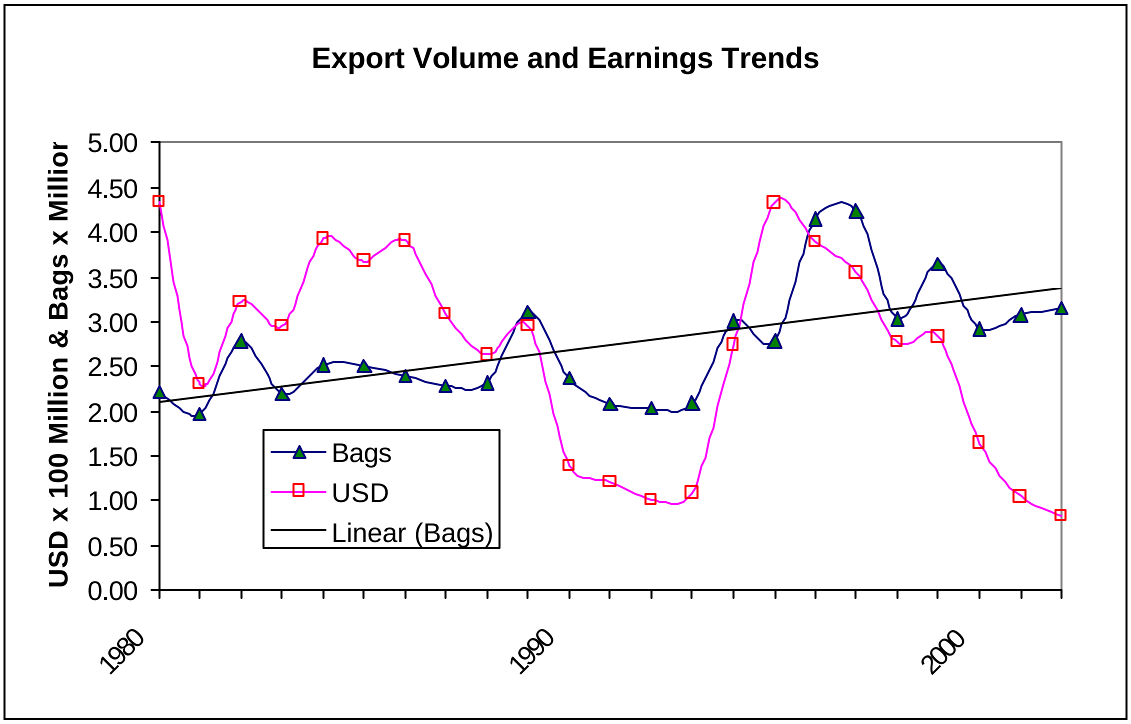

Figure 2, Source: UCDA

Over the past 22 years, Uganda has generated export earnings ranging from just under 100 million USD annually to nearly 450 million USD on coffee sales. The data shows that farmers usually respond to low prices with reduced output and higher prices with increased output. That is, the trend lines more or less move together. That said, it is interesting to note that in the three-year period from MY 2000 - 2002, price and volume trends tend to diverge.

Price and Quality: Figure 3 provides a snapshot of export prices for Ugandan coffee during the fourth quarter of 2002. As can be noted, the Arabicas (on the top half of Figure 3) receive a significantly higher price than do the Robustas listed on the bottom half of the graph.

Bugisu is Uganda's best-known specialty coffee. It is produced in the area around Mt. Elgon, and commands a premium price in the market. Although Bugisu is not sold as a certified appellation, this geography is recognized within the coffee market as producing a unique quality cup.

About half of Uganda's Arabicas are exported as Drugar. The term "Drugar" refers to Arabica coffee that has been sun-dried and the hull removed under a dry process. This is usually done by a mill in rural areas. In some cases, the Drugar's hull is removed by simply beating the dry cherry with a stick, and knocking off the hull. The higher value Bugisu grades are wet milled. The wet mills used for the Bugisu are simple hand-operated machines that remove the hull, yielding a product called parchment. The parchment is then purchased by exporters, remilled, sorted, graded and exported. As the Bugisu is not fermented, the process can be considered a semi-wash.

Robustas are generally priced in terms of their screen size. The larger screen size translates to a larger bean. Most of Uganda's Robusta is exported as screen 15; however, premiums can be realized for larger screens, as denoted by the 22% higher price paid for screen 18, relative to screen 15 in the fourth quarter of 2002.

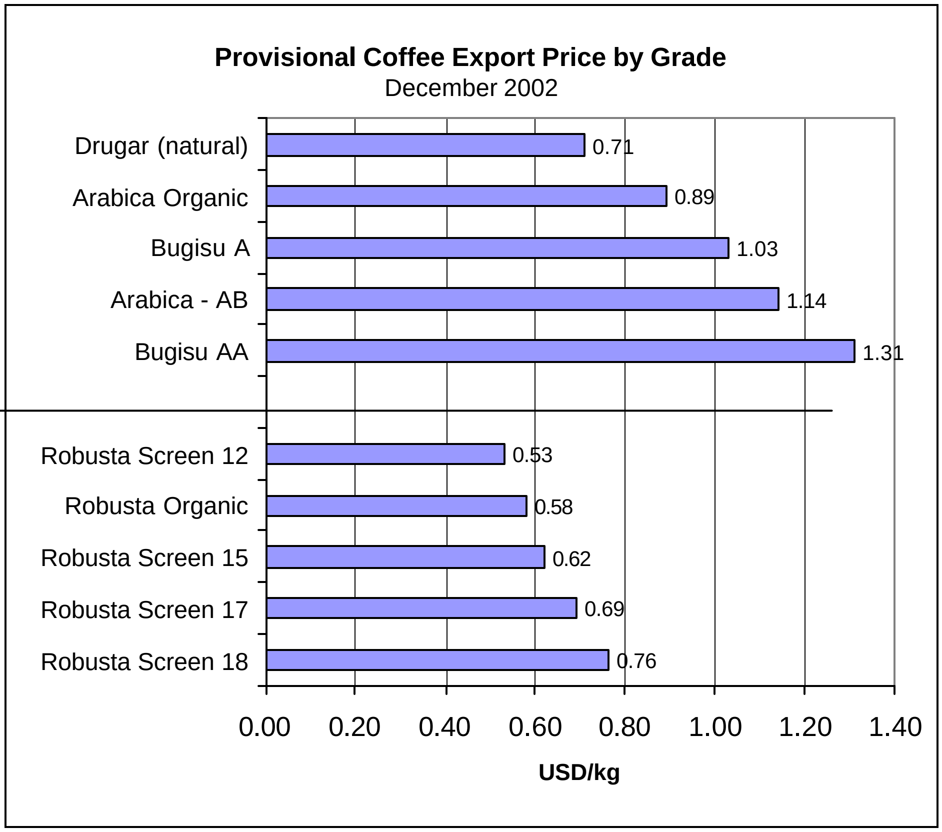

Figure 3, Source: UCDA

It is worth noting that simply getting a coffee certified does not necessarily ensure that it will command a premium price in the market. Cases in point are the organic Arabica and organic Robusta prices noted on the graph above (Figure 3). Both of these are certified organic coffees, yet they are trading in the mid-price range. To increase the value of a coffee, it must have good cup (superior flavor profile), as well as meeting other quality measurements such as acceptable moisture levels, quality milling and sorting, and the absence of extraneous materials. Simply putting a label on a coffee (such as certified organic) in itself is not enough to receive a premium price. Ultimately, potential price is determined by cup quality and other physical characteristics of the shipment.

Geographic Markets: In MY 2001/2002, Uganda shipped 87% of its coffee exports to the EU (see Figure 4). Non-EU Europe imported an additional 6%, making Europe (in general) the destination for 93% of all Ugandan coffee exports.

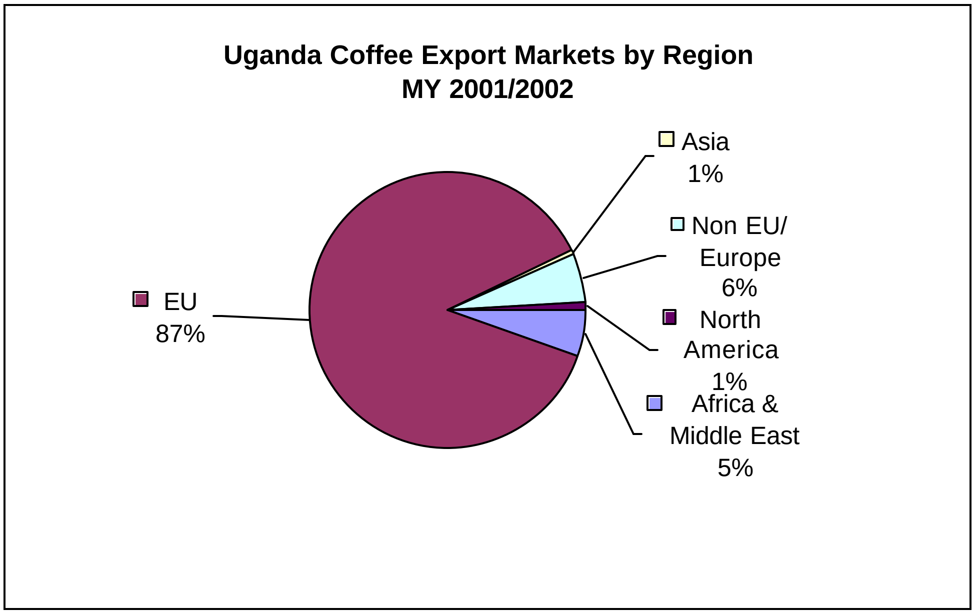

Figure 4, Source: UCDA

The high concentration on the European market has both benefits and detriments. From a market promotion standpoint, being focused in one market allows for concentration of promotional activities. On the other hand, this concentration also implies risk in terms of lack of market diversification.

In MY 2001/2002 Uganda shipped over 80 million USD of coffee to the EU. Given this high level of commercial activity, the Uganda coffee cluster could benefit by opening a promotion/ market intelligence/ commercial representative office in their main market. This office would provide information to importers, roasters and consumers, as well as feeding information back to the Uganda coffee cluster about opportunities and threats in the EU market. As a commercial representative, the office could serve the needs of Uganda SME exporters by helping to work out differences that develop with importers and roasters. The GOU has unused office space available in central London and this may be available for use as the coffee cluster promotion office.

As Uganda develops its specialty coffee sector, it is advisable to concentrate on Europe, but also look beyond Europe for new markets to develop. The UCDA has already started some of this activity by developing a joint venture with the Chinese government to promote coffee sales (through coffeehouses) in and around Beijing.

Market Share: Ugandan export coffee sales are dominated by non-Ugandan firms. Figure 5 (below) examines the market share for coffee exports shipped from Uganda during MY 2001/2002. The ten largest firms held 81% of market share. Seven of these firms are owned by multinationals, and these seven firms controlled 60% of exports. Additionally, two of the local firms (H.M. Nasamba and Sons and Intertrade)[5] were controlled by HSBC Bank, a UK-based financial institution.

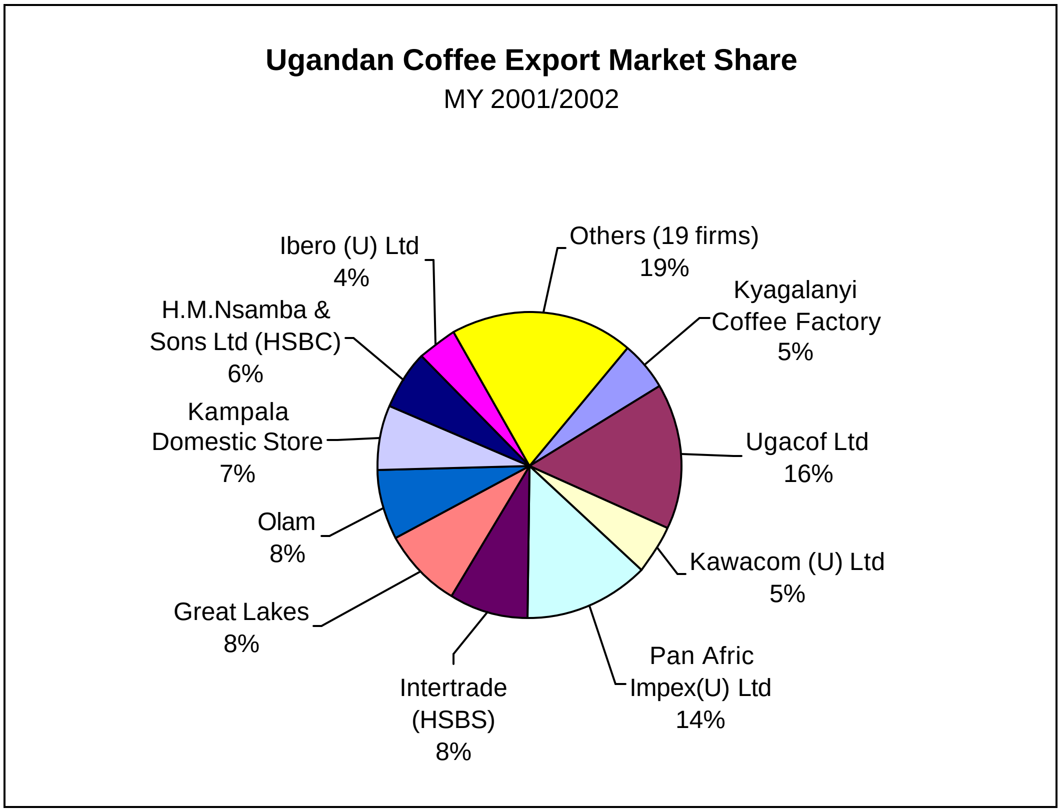

Figure 5, Source: UCDA

In addition to the ten largest firms that control 81% of exports, there are 19 additional firms that average 1% of export sales per year. These smaller firms are all locally owned. Over time, the percentage of market share controlled by local firms has decreased, and the market share for multinationals has increased.

In terms of poverty alleviation for rural Ugandans, it is advisable to encourage the development and strengthening of local exporters. Local firms will tend to invest more in Uganda's economy, rather than exporting its profits offshore.

[5] Nasamba and Sons and Intertrade are being supervised by HSBC, as their level of indebtedness to HSBC and other local banks has pushed them to the point of bankruptcy. Rather than simply writing off these loans, HSBC agreed to come in as an executive management body and work with these firms to repay their debt. HSBC's arrangement allows for a splitting of profits fromcoffee sales whereby HSBC covers the cost of its loan workout department, and the local firm receives funds to pay down their debt and cover operating costs.

There has been some discussion in Uganda's development community about the benefits of investing in capacity building of local companies versus multinational companies. It is argued that local companies are less efficient and less commercially viable than multinationals doing business in Uganda's coffee sector. Undoubtedly, this is a true statement. Multinationals employ fewer people per unit sold than local firms. Multinationals also benefit from a vast international network of market intelligence, sophisticated knowledge in risk management, as well as deep financial capabilities. In terms of business strength and efficiency, multinationals are decades ahead of local companies.

From a development standpoint, this raises a number of questions, including:

- Should Uganda strive to develop its own indigenous value-added/export coffee sector industry, or should it rely on the expertise of foreign firms to carry out these activities?
- Should USAID and other donors favor multinationals over indigenous SME's in their efforts to increase rural incomes?

This report suggests that donors should strive to increase the capacity of indigenous SME's, while continuing work with multinationals. Both of these stakeholders play important parts in addressing rural poverty.

Locally owned SME's are often more likely to plow their profits directly back into the community in the form of urban and rural investments. There is a tendency among multinationals to take their profits out of the country. The typical coffee sector multinational is not interested in investing profits in a Ugandan tourist resort or game lodge, whereas a local company will often diversify its businesses by investing in new local economic activity.

If building local economic/business capacity is one of USAID's goals, it should invest in indigenous coffee sector SME development. Multinational firms have well-developed capacities. In terms of marginal benefits for dollars spent, investments in capacity building of local firms will far outstrip investments in multinationals. If it is USAID's goal to simply increase the incomes of farmers without regard to coffee sector value-addition businesses or exporters, then investing only in multinationals (extension programs) may be a logical path. However, this strategy will limit the upside profit potential for indigenous Ugandan businesses.

ANNEX D Coffee and Conflict Resolution

Coffee production can play a role in conflict resolution in Uganda. Many of the border areas in the west, northwest, and north (particularly Gulu) have had security problems involving civil unrest caused by local guerilla groups. Often, these groups move across borders to avoid capture or confrontation. In places like Gulu, the LRA has terrorized the local population for over a decade.

President Museveni has made defeating rebel groups and restoring civil society to rural areas a priority. USAID can assist in this effort by creating programs that encourage rebels to put down their guns and pick up a hoe. Farming packages that include coffee trees, TA and support to farmer organizations (including possible financing of wet mills and other value-added equipment) can provide former rebels with an alternative to terrorizing local communities.

The UCDA has been working in the Gulu area to promote coffee production since 1997. To date, they have planted approximately 1,600 hectares under shade, and plans are to expand this area over time. This initial project can provide a platform for USAID support in the coffee sector through one of the NGO's operating in the region, such as the International Rescue Committee (IRC).

Coffee can also be produced in Arua, Nebbi, and parts of Moyo District. Arua and Nebbi in particular are known for their good quality coffees. There are areas in these districts that may actually qualify as "coffee appellations". This would allow the coffees to be sold at a premium, as their cup quality would be superior, and the product would be desirable in the specialty market.

ANNEX E Shade Grown Coffee

At the present time, there is no certification program for shade grown coffee in Uganda. If a shade grown coffee program is adopted in the country, it may be necessary to develop some type of certification program through an international partner such as the Smithsonian Shade Grown, Bird Friendly program, or create a regional program through EAFCA, or a domestic program administered through UCDA. To qualify for the Smithsonian certification, coffee must be grown under a rigorous regime that requires organic production, indigenous shade trees (no introduced species are allowed), and requirements for vertical structural diversity and other parameters.

Given the fact that over 90% of Uganda's coffee is sold in Europe, it would make sense to link promotional and certification activities with a European partner. Organizations such as the Royal Society for the Protection of Birds in the U.K. are potential candidates. There are also organizations in France, Germany, and Scandinavia that could also serve as potential alliance partners. These organizations would play a critical role in educating consumers as to the benefits of consuming Ugandan coffees that are shade grown (promote biodiversity) and protect habitat which is used by migratory species that spend half of the year in Europe and the other half in Uganda's coffee growing areas.

If a certification program was to be designed for Uganda or East Africa as a region, consideration must be given to a number of different issues, including the benefits and detriments of using non-indigenous trees (particularly legumes), biodiversity, percent shade cover, ag chemical use, etc. Additionally, the program administrator should develop the ability to monitor certified sites to ensure that they continue production within the shade grown parameters.

Under COMPETE, shade grown coffee was considered any stand that was produced under a canopy of indigenous or introduced trees with a shade cover of 40% or more. This is a minimum requirement; however, it is felt that this would allow for the desired attributes of improved cup quality, improved yields, and allow for the product to be differentiated in the marketplace.

In addition to the possible benefits posed by a higher price received for shade grown coffee, there are also other benefits that include higher yields (which translate to increased farmgate sales), better cup quality for the finished product, reduced plant stress, greater biodiversity, and soil conservation, just to name a few.

In the event that future research shows that the market potential for generating increased profits through the production and certification of shade grown coffee does not, in itself, justify a USAID investment in the activity, planners should also take into consideration the other non-market benefits, such as improved biodiversity, soil conservation, improved coffee quality (cup), and improved crop agronomics.

ANNEX F Developing a Coffee Auction in Uganda

Coffee is a fundamental part of the Ugandan economy. It is the single largest export revenue earner and provides income and employment for nearly 500,000 people throughout the country. Prior to 1991, the coffee sector was dominated by the GOU through the state-owned Coffee Marketing Board (CMB) Ltd. The CMB purchased all the coffee produced in the country and sold it worldwide.

In the post-liberalization period, Uganda's coffee sector evolved to be dominated by a small number of large companies. Many of these firms operate under local names such as Kyagalanyi, Kawacom and Ibero Ltd., but are owned and operated by some of the largest coffee trading companies in the world. This group of multinational companies provides an important function for Uganda's coffee sector; they move the bulk of the nation's coffee crop from their rural depots, through their milling plants and sell the coffee to their subsidiary companies worldwide.

Although this system is efficient at moving Uganda's bulk commodity coffee into the world markets, it is not efficient at providing market opportunities to small and medium size businesses, advancing market transparency, encouraging (paying for) quality coffee production, or promoting Ugandan coffee as a recognized origin in the world market.

To address the foregoing shortfalls in the current marketing system, UCDA, UCFA and UCTF, are interested in developing a private voluntary auction for high value coffees produced in Uganda. The auction will promote market transparency, reduce transaction costs, encourage production of (and payment for) high quality coffee, promote Ugandan coffees internationally and increase accessibility of the export markets to small and medium size businesses and farmer associations.

The mechanics of the auction will work as follows: a coffee consolidator or farmer group will deliver clean, sorted and bagged coffee beans to the Uganda Coffee Auction. The coffee will be graded, samples pulled and made available to coffee buyers who have purchased a "seat" at the auction. When received at the auction facility, the coffee bags will be bar-coded for inventory management purposes and placed in a highly secure warehouse. Anyone with a seat will have the right to bid on stock-lots of coffee at the bi-weekly auction. The seats will sample (cup) the coffee up to 12 days before auction day. The auction will be held two times per month, for example, on the first and third Thursday for the period from September to July. The auction may be closed in August due to low available harvest volumes during that time period.

The seats will bid on stock-lots of coffee at the public auction and an electronic board will display the stock-lot number, coffee origin, quality grade, the bid price in USD/kg and purchasing company in full public view. Once the lot is sold, the buyer will have seven days to settle the account through the auction payment clearing account at a local bank. The bank will deduct auction fees (approximately 3% of gross sales value, half of which is paid by the buyer and half by the seller). Funds will be available to the seller as soon as the buyer's check clears and auction fees are deducted. Payment can be by wire transfer or certified check. Once the buyer's check clears, the warehouse will be notified in writing that payment has been received for a given stock-lot and loading into the buyer's container or rail car can begin. The auction never takes legal ownership of the coffee nor will they be involved in transporting any coffee at any time. The auction will be insured for damage in case of fire, theft and water losses and the auction's Board of Directors will have limited liability coverage in case the auction company's shareholders sue them.

The auction will sell only Arabica and Washed Robusta coffees. The coffee will be sold in relatively small stock-lots (ranging in size from 25 bags to several hundred bags). By allowing the sale of small lots of coffee, the auction will encourage the segregation of high quality coffee and will discourage mixing low grade and higher-grade coffees. This strategy will maximize price and promote Ugandan coffee by delivering quality coffee to the world market.

The auction business plan prepared under the COMPETE Project in late 2001 projected that in the first year of operation, 32,000 bags of coffee would be sold. By YR 4, it was projected that the auction's volume would total 320,000 bags, and would remain constant at this level. One of the biggest challenges an auction would face in Uganda would be achieving volumes that would yield economies of scale. Because of this, there will be a 4 - 5 year start-up period, where the volumes grow each year. It is critical that projects such as UTRADE, PRIME, and APEP strengthen the specialty coffee sector in Uganda over time so it can supply the required volumes to the auction. As volumes of quality coffee grow (as a result of UTRADE, PRIME and APEP activity), so will the auction volume.

The strengths of the auction are that it clearly links quality and price (and rewards quality), provides a transparent price discovery mechanism, promotes Uganda as an origin, creates a low transaction cost, eliminates asymmetric market information, and provides a cash flow/inventory management tool to local traders. It is also accessible and equitable to businesses from SMEs to large trading firms.

The weaknesses that an Arabica/washed Robusta auction face in Uganda are (as already mentioned) volume concerns, a limited amount of washed Robusta, low capitalization of farmer organizations and SMEs, as well as limited local experience in operating a coffee auction.

ANNEX G Scope of Work

Background

The Government's Poverty Eradication Action Plan (PEAP) provides the long-term goal and policy framework for USAID/Uganda's Integrated Strategic Plan (ISP) 2002-2007. Export growth is seen as a sine qua non to the Government of Uganda (GOU)'s top priority of sustaining economic growth at a level of 7% per annum. The GOU has expanded upon the PEAP by laying out a blueprint for economic growth, which emphasizes developing export competitiveness: the Medium-Term Competitive Strategy for Private Sector Development (MTCS). The MTCS articulates a number of priority actions to achieve a sustained growth in the order of 7%. Such growth is needed to achieve the GOU's prime goal of a reducing mass poverty.

USAID/Uganda is in the process of putting into place a 5-year core activity; Uganda-Trade and Diversification of Exports (U-TRADE), to address the needs of Uganda's export sector. U-TRADE will build upon the successful results and approaches of the IDEA, COMPETE and Trade Policy activities. In addition, strong integration with commercial finance, business enabling environment and small business development will be linked to the SPEED program. The primary objective will be to expand and diversify Uganda's export base and penetrate new regional and international markets.

U-TRADE will build upon the MTCS including the work of the Special Task Force on Export Competitiveness that was initiated by the President of Uganda. In addition, U-TRADE will build upon the Economic Growth and Transformation Strategy. This is a document prepared jointly by the GOU, development partners, and the private sector for the Consultative Group meetings. U-TRADE will also build upon recent efforts focused on "Strategic Exports", a joint GOU-donor initiative.

U-TRADE implementation is expected to begin in late spring of 2003. As a result there is a need to work with transition programs to keep up the momentum and maintain USAID's leadership role among the donors involved in promoting private sector development. Under the COMPETE program, and working with the sector working groups represented by both public and private sector stakeholders, sector strategies for Coffee, Fisheries, and Cotton were developed. The three strategies were developed to address four key areas of focus: production, processing, marketing, and sector support (regulations, research, training curricula, and ICT).

Objective

The objective of this review is to support the USAID/Uganda Mission's continued work in developing key clusters in support of the GOU's economic growth targets during the Mission's period of transition to the new core activities. The review will provide information on the current status of implementation by GOU of these sector strategies and initiate a process for continued private-public sector dialogue in the sectors prior to commencement of U-TRADE. It is also hoped that recommendations on best practices and lessons learned will be applied to the design and implementation of U-TRADE.

Scope
The Subcontractor will (1) review the Coffee Competitiveness Strategies supported by USAID/Uganda under the COMPETE Project; (2) identify opportunities to further public-private dialogue between the Coffee Cluster and the Government of Uganda (GOU); and (3) identify specific implementation activities to further cluster development.

Tasks
The Subcontractor shall perform the following tasks, but not limited to:

1. Review the Coffee Competitiveness Strategies for completeness:

   Evaluate the Sector Competitiveness Strategies previously submitted under the COMPETE program. Questions to be answered include:

   (i) Are the Sector Strategies, underlying assumptions, and enabling environment still valid as stated?
   (ii) Are the Sector Strategies being effectively implemented?

If completeness is lacking, advise the Mission on the elements of these three strategies that still need to be completed to obtain approval by the Coffee cluster and GOU.

2. Identify opportunities for implementation support by USAID/Uganda SO7 transition activities (IDEA and SPEED).

   Questions to be answered include:

a) Are the transition activity approaches in these sectors consistent with USAID's best practices for a competitiveness program?
b) What additional opportunities exist for support of implementation by the Mission's SO7 transition activities in this specific cluster? Make prioritized recommendations for transition activity partners.

3. Identify opportunities for transition activities to further public-private dialogue between the Coffee Cluster and the Government of Uganda (GOU).

   Questions to be answered include:

   a) What are the opportunities for public-private dialogue during this transition period that the Mission and the transition activity partners need to support?

   b) Is there 'political will' on the part of the GOU to see the development of the Cluster?
   c) To what extent has the private sector bought-in to the cluster concept?
4. In collaboration with SPEED and/or IDEA or private sector firms, carry out the following specific actions within the sector:

A Coffee Consultant and a Ugandan counterpart will work with SPEED to provide necessary technical assistance to the private firms for the use of wet processing facilities, as may be required.

5. The Subcontractor shall, at a minimum, hold one sector working group meeting for the Coffee Sectors.

Assessment Methodology

The Subcontractor will review the reference documents listed at the end of the Scope of Work, plus other documents that they may find appropriate, to gain an understanding of the background to this activity.

After entrance interviews with USAID/Uganda, the Subcontractor will conduct interviews with Coffee cluster members, respective government officials, partner organizations, donors, and others, as well as review any additional documents that might be available in the field.

Deliverables

The Subcontractor shall deliver a presentation and a draft report of major findings and recommendations under the Coffee sector to CARANA Corporation and USAID. USAID/Uganda will provide comments on the draft reports within a week of receipt. Final reports will be due a week after the Subcontractor receives USAID comments.

An electronic version in Word97/Excel 97 shall be e-mailed to USAID/Uganda. In addition, the Subcontractor should send, via courier, four copies of the final report, plus an electronic version on CD-ROM to USAID/Uganda.

Copies of all reports should be submitted to Robert Otto at CARANA in Arlington, VA.

As appropriate, the Subcontractor will provide CARANA copies of substantive correspondence and documents produced.

Performance Standards

i) The Subcontractor will produce reports that contain actionable recommendations which can/will be successfully implemented by other USAID partners and client organizations.

ii) The final deliverable will be of high quality i.e. clear, concise, accurate, well structured, and easy to comprehend.

Reporting Requirements

The Subcontractor shall produce a report, which will include the following minimum format:

(a) Executive summary stating purpose of the assessment; methodology; findings; lessons learned; conclusions and recommendations.

(b) Table of Contents

(c) Main body of the Report including a discussion of:

(i) The purpose and study questions of the assessment;
(ii) The economic, political and social context of the activities;
(iii) Team composition and methodology;
(iv) Evidence/findings of the study concerning the assessment questions;
(v) Conclusion drawn from the findings, stated in succinct language;
(vi) Recommendations based on the study findings and conclusions, stated as actions to be carried out by transition activities and/or U-TRADE; and
(vii) Provide summaries of the additional activities carried out by the Subcontractor and resulting recommendations.

A Page limit is suggested of 15 pages, plus attachments.

(d) Appendices should include a copy of the assessment scope of work, detailed description of the cluster activities, a list of documents consulted, and individuals and agencies contacted.

Schedule and Logistics

The illustrative schedule for this assessment is as follows:

Week 1-3

- Subcontractor travel to Uganda for fieldwork
- Briefing with USAID/Uganda Mission, submission of work plans
- Interviews and Field Work
- Subcontractor present findings & draft report
- USAID/Uganda Mission provides comments to Subcontractor
- Expatriate Subcontractor Depart
- Final report due to USAID/Uganda

The Subcontractor will be responsible for making all logistical arrangements including international and in-country travel.

Reference Documents

a. USAID/COMPETE Final Report (CARANA Corporation)
b. USAID/COMPETE Sector Strategy Reports for Coffee, Fisheries, and Cotton (Draft)
c. Trade Policy Final Report (Nathan Associates)
d. SPEED and IDEA Quarterly reports
e. Medium-Term Competitive Strategy for Private Sector Development (MTCS)
f. Economic Growth and Transformation Strategy
g. Strategic Exports in Uganda: Performance and Growth Prospects - Synthesis Report

Summary of USAID/Uganda So7 Activities Listed in Sow

Investment in Developing Export Agriculture (IDEA):

The IDEA project goal is to increase rural household incomes. The main intermediate results under IDEA are increased value of selected non-traditional agricultural exports (NTAEs), increased production of selected food products, and increased use of financial services by rural households. IDEA works to expand the production and exports of both low value (LV) food crop exports (primarily maize and beans), and of high value (HV) crops (such as flowers, fresh produce, cocoa, papain and vanilla).

Support for Private Enterprise Expansion and Development (SPEED):

SPEED was designed to meet the needs of micro, small and medium enterprises (MSMEs) and focuses on access to finance and business skills development. Through the SPEED project, USAID seeks to increase access to financial services, create and expand agricultural and non-agricultural enterprises, and strengthen legal and regulatory frameworks for business development in the SME and microfinance sectors. Activities implemented under the four components of the project — SME finance, microfinance, business development services (BDS), and institutional environment — support these goals. Specifically, SPEED works with SMEs, microfinance institutions (MFIs), and commercial banks to strengthen their capacities in order to meet the financial needs of the "missing middle." The project works with BDS providers to offer quality and demand-driven services that address the business needs of microenterprises, SMEs, and agricultural enterprises. Finally, SPEED works in the policy arena to address constraints to microenterprise and SME development.

Competitive Private Enterprise and Trade Expansion (COMPETE):

The COMPETE Project was designed to respond to Uganda's urgent need to improve the export competitiveness of its private enterprises in international markets so as to increase its foreign exchange earnings and boost domestic economic activity and employment. In this effort, USAID supported the Government of Uganda's Medium-Term Competitive Strategy for the Private Sector by providing technical assistance to the government and private sector to strengthen the capacity of the private sector to compete in global markets. Working with the Government of Uganda's Special Task Force on Export Competitiveness, the COMPETE team selected three sectors: coffee, fish, and cotton each of which contribute substantially to export earnings and rural incomes. A fourth sector, information and communications technology, was selected as a crosscutting sector to strengthen the three sectors in achieving international competitiveness.

Trade Policy Capacity Building Program (TPCBP):

The Trade Policy Capacity Building Project was funded by USAID under the auspices of the PSF. The project enabled Uganda's private and public sector stakeholders address current and upcoming trade policy issues—such as those arising from the World Trade Organization (WTO), African Growth and Opportunity Act (AGOA) and regional trade agreements. Specific project components included: (i) training to provide information on Uganda's existing international and regional commitments and prepare stakeholders for ongoing trade negotiations; (ii) specialized technical assistance working with key public and private sector institutions on trade-related assignments such as understanding WTO rules on customs valuation; (iii) a consultative process through established specialized private sector committees' on agriculture, manufacturing, and service sectors; and (iv) a public awareness campaign in collaboration with the Joint Integrated Technical Assistance Program (JITAP) of the WTO, UNCTAD, and ITC.

Work Week:

The Subcontractor is authorized up to a six-day workweek in the field with no premium pay.